

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE APPLICATION OF LAKEWOOD)	
VALLEY SEWER CO., INC. FOR A)	
RATE ADJUSTMENT PURSUANT TO)	CASE 93-279
THE ALTERNATIVE RATE FILING)	
PROCEDURE FOR SMALL UTILITIES)	

O R D E R

On August 11, 1993, Lakewood Valley Sewer Company, Inc. ("Lakewood") filed its application for Commission approval of a proposed increase in its rates for sewer service. The proposed rates would produce an increase in annual revenues of \$29,872, an increase of 74.26 percent over test period normalized revenues from rates of \$40,226.

The Commission Staff ("Staff") performed a limited financial review of Lakewood's operations for the test period, the calendar year ending December 31, 1992. Based on this review, a Staff Report was issued on November 12, 1993, recommending that Lakewood be allowed to increase its annual revenue from rates by \$17,969, or 44.67 percent.

To reduce soil erosion and eliminate muskrat damage, Lakewood proposed to install rip rap around its lagoon at a cost of \$18,000. In its report, Staff recommended that Lakewood be allowed to collect a monthly surcharge of \$1.35 per customer for a 60-month period to finance the installation of the rip rap. Staff estimated

that the surcharge would result in monthly collections of \$300, or \$18,000 at the end of the 60-month period.

The Commission received numerous comments and complaints from Lakewood's customers. The following requested and were granted intervention in this proceeding: Richard Van Horne; Michael Boone; Kevin Kincaid; Michael True; William Marcum; and the Attorney General's Utility Rate and Intervention Division ("Attorney General").

The Intervenor requested and a formal hearing was held on December 15, 1993, at the Commission's offices at Frankfort, Kentucky. Mr. Van Horne was represented by counsel; Michael Boone, Kevin Kincaid, and Michael True appeared on their own behalf. At the hearing, Michael Boone and Michael True gave preliminary statements and Mr. Van Horne provided testimony.

The following are the Commission's discussions and findings on the issues raised by the Intervenor in this proceeding:

HOURLY RATE OF F&W OPERATIONS

The Attorney General claims that the hourly rate paid to F&W Operations for the maintenance performed by Frank Wethington, the owner of Lakewood, is excessive. According to the Attorney General, the maintenance performed by Mr. Wethington is billed at an hourly rate of \$25.00; but if another F&W Operation employee performs the task the rate is \$7.00 per hour. The Attorney General argues that the maintenance work performed by F&W Operations has a market value of \$7.00 per hour and, therefore, requests the hourly

rate charged for Mr. Wethington's services be reduced to that amount.¹

Mr. Wethington is a certified plant operator and is the only F&W Operations employee whose services are billed to Lakewood at an hourly rate.² John Beckin, who is not a certified plant operator, works roughly 44 hours per week for F&W Operations and is paid \$7.00 per hour.³ Mr. Beckin performs the routine maintenance that does not require the expertise of a plant operator.

Therefore, the Commission concludes that the \$25.00 hourly rate for Mr. Wethington's services as a plant operator is reasonable. Furthermore, the Commission advises Mr. Wethington to utilize non-certified F&W Operations employees to the greatest extent possible.

OWNER/MANAGER FEE

The Attorney General claims that Mr. Wethington currently operates 9 treatment plants for which he is paid \$72,309 per year. The Attorney General requests the Commission to look at the "big picture" in analyzing the owner/manager fee Lakewood pays to Mr. Wethington. The Attorney General proposes that Mr. Wethington's total level of compensation received for operating the 9 treatment plants be reduced by 50 percent and then a reasonable amount should be allocated to Lakewood.⁴

¹ Brief of the Attorney General, pages 1 through 3.

² Transcript of Evidence, page 120.

³ Id.

⁴ Brief of the Attorney General, pages 3 and 4.

The Attorney General's proposal to consider the other eight treatment plants requires the Commission to review information that it considers to be beyond the scope of this proceeding. Furthermore, Mr. Wethington operates the treatment plants that he owns as stand-alone entities which must be treated separately for rate-making purposes.

SECRETARIAL

In his brief, the Attorney General states that the secretarial fee paid by Lakewood to Mr. Wethington's wife is excessive. Because the financial statements and income tax returns are prepared by Lakewood's accountant, and its billing is performed by Oldham County Water District ("Oldham County"), the secretary performs very few tasks. The Attorney General proposes to eliminate the secretarial salary of \$1,200 because it is included in the management fee paid to Mr. Wethington.⁵

Lakewood contends that Mrs. Wethington spends approximately 250 hours per year performing secretarial services for Lakewood. Since the annual salary is \$1,200, she receives an average hourly wage of \$4.80. Lakewood claims this is far below the normal rate paid for an experienced secretary.⁶

The secretarial duties performed by Mrs. Wethington for Lakewood are outlined in Exhibit 8 of the Transcript of Evidence. Based upon its review of the duties performed by Mrs. Wethington, the Commission concludes that her duties are separate from those

⁵ Brief of the Attorney General, pages 5 and 6.

⁶ Petitioner's Brief in Support of Rate Increase, pages 5 and 6.

Mr. Wethington performs to receive his management fee and thus, the secretarial fee should not be eliminated.

CUSTOMER BILLING AND COLLECTION FEE

As previously mentioned, Lakewood's customer billing and collection was performed by Oldham County. The Attorney General argues that Oldham County arbitrarily increased the monthly billing fee it charges Lakewood from \$1 to \$2 per customer. Because Mr. Wethington did not protest the increase, the Attorney General requests the Commission order Mr. Wethington to make a reasonable effort to secure a more favorable arrangement with Oldham County.⁷

Lakewood argues that if it were to discontinue using Oldham County for customer billing and collection, then it would be forced to maintain separate records, maintain an accounts receivable journal, employ a full-time bookkeeper, and expend additional amounts for postage, office stationary, and envelopes. Accordingly, Lakewood's position is that the most economical method to provide this service is to continue to utilize Oldham County.⁸

Presumably, if Lakewood were forced to hire a full-time bookkeeper to perform its billing function at the minimum wage of \$4.25 per hour it would result in an annual cost of \$8,840, which far exceeds the customer billing and collection expenses paid in the test period. Based on the evidence of record, the Commission has determined that the billing and collection fee paid to Oldham County is reasonable.

⁷ Brief of the Attorney General, page 6 and 7.

⁸ Petitioner's Brief in Support of Rate Increase, page 2.

COMPETITIVE BIDS

According to the Attorney General, Lakewood's competitive bidding process is invalid. This is because Rick Mills, the owner of River City Sewer Service and one of the bidders, has worked for F&W Operations on the projects that were awarded by Lakewood.⁹

Lakewood contends that when it awarded the routine maintenance contract it solicited bids from F&W Operations, River City Sewer Service, and Andriot Davidson. Because F&W Operations submitted the lowest bid, it was awarded the contract. Lakewood claims that it solicits bids for major projects, but due to time constraints and the cost to solicit bids, they are not taken on every project. According to Lakewood, there are no funds available to pay Mr. Wethington for bid solicitation; therefore, Mr. Wethington takes care of the problem the best he can.¹⁰

In its report, Staff recommended that an owner/manager fee of \$2,400 be paid to Mr. Wethington as compensation for the managerial services he provides to Lakewood. The solicitation of bids would be included in the services covered by the owner/manager.

The Intervenor's pointed to the installation of a flow meter and the painting of tanks as maintenance projects that would require the solicitation of bids. The Commission concludes that in this instance the amounts Lakewood paid for the F&W Operations services are reasonable. However, the Commission advises Lakewood that in the future it should modify its bidding process to include

⁹ Brief of the Attorney General, page 7.

¹⁰ Petitioner's Brief in Support of Rate Increase, page 4.

companies that are not connected to either Mr. Wethington or F&W Operations. Bids should also be solicited for projects that are in the price range of those questioned at the hearing.

ACQUISITION ADJUSTMENT

The Attorney General argues that the Commission should not permit Lakewood to recover the plant acquisition adjustment of \$6,445 from its ratepayers.¹¹ Staff based its recommended depreciation expense on the original cost of Lakewood's utility plant in service of \$105,715 in accordance with regulatory practice. Therefore, the plant acquisition adjustment will not be recovered from Lakewood's ratepayers.

MANAGEMENT ISSUES

The Attorney General requests the Commission to perform a management audit of Lakewood because of Lakewood's history of poor management decisions. The Attorney General believes a management audit would prove invaluable to a utility of Lakewood's size.¹²

In this instance, a management audit would be of dubious benefit because of the small size of Lakewood and the limited number of management and operational decisions at issue. The Commission finds that the traditional rate-making process should be adequate to review these decisions. Moreover, the Commission's Financial Audit Branch plans to perform a financial audit of Lakewood, including a review of internal controls, in the near future.

¹¹ Brief of the Attorney General, page 8.

¹² Brief of the Attorney General, pages 8 and 9.

The Commission, after considering the evidence of record and being otherwise sufficiently advised, finds that:

1. The recommendations and findings contained in the Staff Report are supported by the evidence of record, are reasonable, and should be adopted as the findings of the Commission in this proceeding and are incorporated by reference as if fully set out herein.

2. The rates proposed by Lakewood in its application will produce revenues in excess of that found reasonable herein and should be denied.

3. Lakewood should be authorized to assess a monthly surcharge of \$1.35 per customer for a period not to exceed 5 years, or until \$18,000 has been collected. The proceeds of this surcharge should be invested in a separate interest bearing account and used solely for financing the installation of the rip rap at Lakewood's lagoon. If the sum total of the surcharge proceeds and any accumulated interest earned thereon reaches \$18,000 before the 60-month period ends, Lakewood should cease immediately assessing the surcharge.

4. Lakewood should list the surcharge as a separate line item on each customer's bill.

5. Lakewood should submit to the Commission, within 14 days from the end of each month, a monthly activity report containing the following information:

- a. the monthly surcharge billings and collections.
- b. the monthly bank statement.

c. payments from the account.

6. Lakewood should install the rip rap at its lagoon no later than August 31, 1994. Lakewood should be aware that the Staff will be performing an inspection of Lakewood's lagoon to ensure that the rip rap has been installed.

7. Failure to submit the required report or to install the rip rap within the prescribed time should result in the forfeiture of Lakewood's surcharge and the refund of the proceeds plus interest to the customers.

8. The rates in Appendix A are the fair, just, and reasonable rates for Lakewood and will produce gross annual revenues of \$58,208. These rates will allow Lakewood sufficient revenues to meet its operating expenses and provide for future equity growth.

IT IS THEREFORE ORDERED that:

1. The rates proposed by Lakewood in its application are denied.

2. Lakewood is hereby authorized to assess a monthly surcharge of \$1.35 per customer for a period not to exceed 5 years, or until \$18,000 has been collected. The proceeds of this surcharge will be invested in a separate interest bearing account and used solely for financing the installation of the rip rap at Lakewood's lagoon. If the sum total of the surcharge proceeds and any accumulated interest earned thereon reaches \$18,000 before the 60-month period ends, Lakewood will cease immediately assessing the surcharge.

3. Lakewood shall list the surcharge as a separate line item on each customer's bill.

4. Lakewood shall submit to the Commission, within 14 days from the end of each month, a monthly activity report containing the following information:

- a. the monthly surcharge billings and collections.
- b. the monthly bank statement.
- c. payments from the account.

5. Lakewood shall install the rip rap at its lagoon no later than August 31, 1994.

6. Failure to submit the required report or to install the rip rap within the prescribed time, shall result in the forfeiture of Lakewood's surcharge and the refund of the proceeds plus interest to the customers.

7. The rates in Appendix A are approved for service rendered by Lakewood on and after the date of this Order.

8. Within 30 days of the date of this Order, Lakewood shall file with the Commission its revised tariff setting out the rates approved for service rendered on and after the date of this Order.

Done at Frankfort, Kentucky, this 6th day of June, 1994.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:


Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 93-279 DATED JUNE 6, 1994.

The following rates and charges are prescribed for the customers in the area served by Lakewood Valley Sewer, Inc. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

Customer Class

Rate Per Unit

Single Family Residential

\$21.85

Monthly Surcharge

\$1.35 for a period of 60 months or until \$18,000 has been collected.